

# PHILIPPINES ECONOMIC WRAP-UP

NOVEMBER 18 - DECEMBER 01, 2000

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Summary  
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Despite unrest in Mindanao and other problems the Philippine economy continued to grow in the third quarter, with GDP accelerating 4.8% over the third quarter of 1999; government officials hope the rate can be sustained in the fourth quarter despite political turmoil. Imports in September were also up 16%, surprising many analysts after 5 consecutive months of decline. In other news, the peso has been more stable, with volatility reduced. Interest rates seem to be 'normalizing' despite a ballooning budget deficit (now nearly 53% over the original target). The government finally scored a small victory with the privatization of Philphos, but the sale of government shares in Philippine National Bank to local tycoon Lucio Tan seems to be going nowhere.

Readers should note that we will publish the "Wrap-Up" on December 8, 15, and 22; we will not publish the "Wrap-Up" on Friday, December 29.

These weekly reviews are available on the Embassy's web site (<http://usembassy.state.gov/manila>). We provide a longer and more detailed review of the Philippine economy in our October Economic Outlook, which is also available on our web site.

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**FOREX REPORT**  
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As traders adopt a 'wait-and-see' attitude regarding the ongoing impeachment process facing Philippine President Joseph Estrada, the peso continues to hover just below the P50/US\$ mark. The peso has also seen its trading volatility reduced; from fluctuations of up to P3.00/\$ a day when the scandal first broke, the trading range has now shrunk to a more reasonable P0.20-0.30/\$. In addition to the renewed focus on fundamentals (rather than political sentiment), the peso has also been strengthened by seasonal inflows of remittances from overseas Filipino workers (OFWs). On Friday, December 1, the peso closed at P49.56/USD.

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Exchange Rate Tables  
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Date	Weighted Average (Pesos/US\$)	Closing (Pesos/US\$)	Volume (Million US\$)
	-----	-----	-----
OCT 23	48.894	48.960	76.7
24	49.143	49.205	99.5
25	49.633	49.650	155.0
26	50.033	50.400	58.5
27	51.015	50.080	46.0
OCT 30	51.427	51.480	77.8
31	51.680	51.000	28.5
NOV 01	Markets Closed		
02	Markets Closed		
03	Markets Closed		
NOV 06	48.895	48.050	133.5
07	48.911	49.250	133.5
08	50.189	50.100	154.5
09	50.414	49.950	185.8

10	49.661	50.200	166.0
NOV 13	50.314	50.350	125.5
14	49.885	49.830	93.5
15	49.717	49.800	65.5
16	49.904	49.890	124.4
17	49.915	49.860	79.5
NOV 20	49.834	49.815	68.1
21	49.554	49.490	97.0
22	49.465	49.120	156.7
23	49.151	49.380	113.2
24	49.544	49.930	131.5
NOV 27	49.440	49.410	150.0
28	49.393	49.520	93.1
29	49.590	49.630	174.4
30	Markets Closed		
DEC 01	49.667	49.560	142.0

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Source: Bankers Association of the Philippines

#### **CREDIT MARKET REPORT**

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With reduced pressure on the Philippine peso, credit markets seem to have returned to a more normal footing for now. The Treasury Bureau had successfully used rejections and reduced T-bill sales for much of the year to keep domestic interest rates low, hoping this would continue to spur economic growth. However, given growing fears of inflation, political uncertainty, and a ballooning fiscal deficit, upward pressure on rates grew significantly. When the Treasury finally allowed rates to adjust on November 6, the rate on 91-day bills leapt almost 700 basis points. It seems that markets overshot somewhat; at the November 27 T-bill auction rates on the 91-day bill had settled back to 14.806%. The rate for the 182-day bill was set at 15.168%; and the rate on the 364-day bill is 15.235%. The auction was oversubscribed; P7.65 billion worth of tenders were received for the P4 billion worth of bills on offer. In light of the more favorable environment, the Treasury Bureau has ceased

issuing 'cash management bills'. Given the improved environment, there is speculation that the policy-making Monetary Board of the Bangko Sentral ng Pilipinas (BSP) will soon move to reduce its overnight rates. However, Monetary Board members have indicated they will wait to see November inflation figures before making such a move.

Encouraged by a warmer reception in recent weeks to longer-term government paper, the government decided to launch 25-year Treasury bonds on November 28 (Tuesday), after volatile rates prevented it from selling the bonds in October. Mainly targeted for institutional investors with long-term investment needs (i.e., insurance firms, mutual funds, trust companies), the government had expected to raise about P2 billion from the offering. It received tenders of almost P6.4 billion and accepted about P5.3 billion at a coupon rate of 18.25%. That rate, according to DOF officials, fell within government expectations of 18-18.5%. (There are no immediate plans as yet for another offering.) DOF officials said the 25-year T-bond represents the longest tenor in Asia after Japan (which has issued 30-year bonds). The longest-issued maturity before that were 20-year bonds (floated in April 1997) at a 14.38% coupon rate.

The improved atmosphere also generated positive results at the renewed weekly T-Bond auction. (T-bond auctions are normally held on Tuesdays; this one was held on Wednesday, November 30 to accommodate the 25-year bond auction noted above.) T-bond auctions were suspended two months ago due to poor appetite for long-term paper. P3-billion worth of 2-year bonds were offered; against P3.462 billion of tenders the Treasury Bureau awarded P2.862 billion. The rate for the 2-year paper was set at 16.0%, 350 basis points higher than its last offering.

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Domestic Interest Rates (in percent)  
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Treasury Bills  
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Auction Date	91 days	182 days	364 days
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OCT 23	all bids rejected		
OCT 30	no sales	no sales	18.926

NOV 06	16.723	17.229	17.389
NOV 13	16.292	17.022	16.863
NOV 20	15.637	15.749	15.977
NOV 27	14.806	15.168	15.235

Source: Bureau of the Treasury

#### Prime Lending Rates of 15 Expanded Commercial Banks

Date of Survey	Average	Range
OCT 19	14.3294	10.924 - 24.50
OCT 26	15.9834	11.625 - 24.50
NOV 09	18.5480	14.50 - 21.172
NOV 16	18.6764	14.50 - 21.50
NOV 23	18.4160	14.50 - 21.367
NOV 29	18.2152	14.50 - 21.00

Sources: Bangko Sentral ng Pilipinas; Press reports

#### STOCK MARKET REPORT

Trading volumes were helped by some block trading early in the two week period, but overall interest in the Philippine stock market was waned somewhat in the face of weak corporate profits. There are some indications that foreign portfolio capital has done some bargain hunting in the market, but volumes remain fairly modest. The 33-share Philippine Stock Index (PHISIX) closed at 1386.25 on December 1.

#### Philippine Stock Exchange Index (PHISIX) and Value of Shares Traded

Date	PHISIX Close	Value (Million pesos)
OCT 23	1267.69	445
24	1282.42	481
25	1294.37	616
26	1293.63	554

27	1284.88	812
OCT 30	1284.66	359
31	1287.85	536
NOV 01	Markets Closed	
02	Markets Closed	
03	Markets Closed	
NOV 06	1500.10	3840
07	1512.58	2084
08	1478.42	1768
09	1488.79	1006
10	1488.95	857
NOV 13	1455.94	695
14	1469.58	724
15	1469.20	3703
16	1468.44	2371
17	1470.52	2531
NOV 20	1465.10	2496
21	1449.00	757
22	1456.65	498
23	1447.74	599
24	1442.27	599
NOV 27	1434.25	448
28	1418.04	655
29	1404.83	695
30	Markets Closed	
DEC 01	1386.25	1100

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Source: Philippine Stock Exchange

### 3RD QUARTER ECONOMIC GROWTH ACCELERATES

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According to new government estimates, the Philippine economy held its own during the third quarter despite internal and external pressures and uncertainties (i.e., the Mindanao conflict, a weakening peso, and oil price increases). Third-quarter GDP expanded by 4.8% year-on-year, from 4.5% growth in the second quarter. GNP growth

-- which accelerated from 4.4% in the second quarter to 5.7% in the third -- received a boost from a 20.3% expansion in net factor income flows. Although factor inflows (mainly workers' remittances in peso terms) grew at a somewhat slower pace (20.5%) than in the second quarter (23.9%), outflows (for interest expense and property-related payments) slowed more markedly. The comparable third-quarter 1999 growth figures were 3.8% for both GDP and GNP.

On the demand side, the third-quarter numbers showed stronger rates of expansion for personal consumption, exports, government consumption, and investments. Investments (up 4.7% year-on-year) broke from four consecutive quarters of negative year-on-year growth -- which reflected some improvement in durable-equipment demand but, mainly, smaller net drawdowns from inventories compared to 1999's third quarter.

As for output, only the service sector (up 4.9%) did not better its second-quarter growth performance (5%), reflecting slower rates of expansion for finance, real-estate, and private services. Both agriculture (up 5.5%) and industry (up 4.4%) surpassed their respective second-quarter growth rates of 4.8% and 3.5%, respectively. In the industrial sector, improved third-quarter performances by the manufacturing and utility sub-sectors managed to pull up the continued weakness in construction activity.

On a cumulative nine-month basis, real GDP expanded 4.2% year-on-year and GNP by 4.5% (compared with comparable 1999 growth rates of 2.7% for GDP and 3.1% for GNP). That faster overall expansion has been spurred mainly by the private non-agricultural sector. Agricultural growth slowed to more normal levels after 1999's rebound from drought-induced 1998 losses and the government moved from pump-priming to fiscal tightening. Despite unsettling fourth-quarter political developments (the "jueteng" gambling scandal) which have affected the peso, domestic interest rates, and investor confidence, the government hopes to hit at least 3.4% GDP growth in the fourth quarter (the rate needed to achieve the lower end of the government's targeted full-year growth range). With the year drawing to a close, private economists are

more concerned over the potential impact of protracted political uncertainties on prospects for the new year.

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YEAR-ON-YEAR GDP AND GNP GROWTH  
(Real Terms, In %)  
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	1999		2000	Jan - Sep	
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	Q3	Q2	Q3	1999	2000
GDP	3.8	4.5	4.8	2.7	4.2
Net Factor Income	4.2	3.6	20.3	10.5	10.1
Inflow	7.4	23.9	20.5	6.6	19.4
Outflow	12.3	51.4	20.8	1.4	32.9
GNP	3.8	4.4	5.7	3.1	4.5
Industrial Origin					
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Agriculture	5.3	4.8	5.5	5.7	3.3
Industry	2.5	3.5	4.4	(0.1)	4.1
Mining/Quarry	(13.3)	9.1	0.5	(14.3)	9.5
Manufacturing	2.4	6.2	6.7	0.8	6.3
Construction	5.2	(8.6)	(5.7)	(2.5)	(6.4)
Elect, Gas, Water	4.5	4.3	5.1	2.4	4.6
Services	4.3	5.0	4.9	3.8	4.6
Transp, Communic.	5.8	10.9	11.0	4.7	9.8
Trade	5.8	6.5	6.5	4.4	5.9
Finance	1.0	1.9	1.3	1.8	1.2
Real Estate	0.8	1.6	1.4	0.4	1.6
Private Serv.	5.7	4.3	3.5	5.7	4.3
Gov't Serv.	2.9	0.9	0.9	3.5	0.8
Expenditure Share					
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Personal Consumption	2.5	3.2	3.5	2.5	3.3
Gov't Consumption	3.1	0.8	1.8	5.0	0.3
Capital Formation	(0.6)	(0.7)	4.7	(0.6)	0.5
Fixed Capital	1.7	(2.8)	(0.6)	(2.6)	(1.6)
Construction	6.3	(7.8)	(4.4)	0.0	(5.4)
Durable Equip.	(3.7)	2.8	3.4	(5.9)	2.9

Change in Stocks (Billion Pesos)	(3.9)	(1.6)	(1.6)	(5.9)	(2.7)
Exports a/	11.5	13.7	18.3	2.0	14.5
Less: Imports a/	1.5	(3.8)	(2.9)	(5.3)	(1.9)

a/ Goods and services

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Source: National Statistical Coordination Board

#### **SEPTEMBER IMPORTS UNEXPECTEDLY REBOUND BY 16%**

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Merchandise imports in September, after falling for five straight months year-on-year, rebounded by an unexpected 16 percent to \$2.97 billion from the previous year's comparable \$2.56 billion. Some economists attribute September's rebound to inventory building ahead of the holiday season, while other industry analysts perceive this surprising jump as a stop-gap measure to augment dwindling production. For the first three-quarters of the year, imports posted a weak 2.2 percent growth over the first nine months of 1999. Industrialist Raul Concepcion, head of the Federation of Philippine Industries, has said that roughly half of its members have postponed procurement of key inputs and scaled down operations due to the weakening peso and rising interest rates. Just recently the 40-year old domestic assembler of Yamaha motorcycles, Norkis Trading Company, has announced the company is 'temporarily' shutting down part of its operations effective December this year. Norkis, which imports at least 90% of required components, has actually stopped importation since November due to the depreciating peso, which translated to (at least) a 25% increase in production cost. At a 20% profit margin, continuing the assembly business is a losing proposition, a Norkis spokesperson said.

Skyrocketing crude oil prices continue to distort import data. Excluding payments for mineral fuels, September demand for foreign goods logged a growth rate of just 10% over September a year ago. It remains to be seen if the September growth is just an aberration or whether the electronics sector has finally bottomed out, a private

securities economist commented. Growing imports from Taiwan (up 99%) and Japan (up 22.3%), major sources of electronic raw materials and passenger car parts, make up for declining imports from the U.S. (down 4.5%) and Korea (down 33.5%). Latest trade figures from the National Statistics Office (NSO) show that some investments in the electronic manufacturing sector fueled year-on-year import growth in September. Other interesting information gleaned from the NSO data include:

-- Some specialized machinery (up 40% by value) was brought in mostly by new and expanding investors in special economic zones. This was confirmed by a recent report by the Philippine Economic Zone Authority (PEZA) that investments in ecozones have more than doubled to P70 billion (\$1.6 billion) in the first ten months of the year relative to the same period a year earlier.

-- Demand for material inputs required for the manufacture of electronic devices and components surged by 39% to \$437 million. Imports in this key sector had fallen sharply over the previous months as declining world prices for earlier-technology devices slowed import-dependent exports.

-- The oil import bill jumped 82% to \$382 million, mainly due to skyrocketing prices of oil in the world market -- now at \$30 per barrel from only \$10 a year ago. Import volume has actually declined by 7% in the first eight months of the year compared to last year's level.

-- Rice imports worth \$28 million (up from just \$2 million in 1999) arrived in September.

Table I

----- PHILIPPINE FOREIGN TRADE PERFORMANCE January - September 2000 (FOB Value in Million \$) -----			
	Exports	Imports	BOT
Jan 1999	2,581	2,400	181
Feb	2,569	2,257	312
Mar	2,702	2,656	46
Apr	2,346	2,599	(253)
May	2,747	2,533	214
Jun	2,857	2,671	186
Jul	2,851	2,792	59

Aug	3,212	2,661	551
Sept	3,693	2,555	1,138
Jan-Sept	25,558	23,125	2,434
Jan 2000	2,717	2,651	65
Feb	2,902	2,483	419
Mar	2,988	2,742	247
Apr	2,668	2,528	140
May	2,931	2,437	494
Jun	3,410	2,494	916
Jul	3,219	2,675	544
Aug	3,529	2,643	886
Sept	3,502	2,972	530
Jan-Sept	27,867	23,627	4,240

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Source: National Statistics Office

Table II

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Philippine Imports by Major Groups  
September 2000  
(FOB Value in Million \$)  
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	September		Pct Growth
	1999	2000	(Y/Y)
T O T A L	2,555	2,972	16.3
Capital Goods	1,059	1,099	3.8
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Telecom Eqpmt. and			
Elect. Machinery	649	601	(7.4)
Power Generators and			
Specialized Mach.	177	248	40.1
Other capital goods	233	250	7.3
Raw Materials and			
Intermediate Goods	984	1,090	10.8
-----	-----	-----	
Mat/Acc for Mafr			
Of Electronic eqpmt.	315	437	38.7
Artificial Resins	54	64	18.5
Other material inputs	615	589	(4.2)
Mineral Fuel	210	382	81.9
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Petroleum Crude	161	308	91.3
Other Products	49	74	51.0
Consumer Goods	210	256	21.9
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Dairy Products	28	39	39.3
Passenger Cars and Motorized cycles	28	36	28.6
Rice	2	28	1,300.0
Other Consumer Goods	152	153	0.6
Other Transactions	92	145	57.6
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Source: National Statistics Office

#### **TEN-MONTH FISCAL DEFICIT SWELLS TO P95.5 BILLION**

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The national government's fiscal deficit widened further from P83 billion in September to P95.5 billion at the end of October 2000. After having breached the P62.5 billion full-year target in August, the government was hoping to contain the deficit within P90 billion by the end of the year. Budget officials now say that cash releases will be programmed carefully during the remaining months of 2000 to keep the full-year deficit from breaching the P100 billion mark. However, it remains to be seen just how much more the government can withhold given an already tight spending plan to begin with, as well as emerging pressures on interest payments from a weak peso and recent increases in domestic interest rates. For example, exasperated Commission on Election (Comelec) officials complained on national television that delayed budget releases were hampering preparations for the May 2001 elections.

Private analysts (as well as Embassy Manila) do not see the government's performance ending this year as better off than in 1999 -- during which the national government had originally envisioned a P68.4 billion deficit-ceiling but eventually ended with a P111.7 billion fiscal gap. About this time last year, the ten-month deficit stood at P96.8 billion (very close to 2000's P95.5 billion January-October level). With another two months to go

and no immediate revenue relief in sight, a number of estimates see the fiscal deficit ballooning to P120 billion or more by the end of 2000. Budget and finance officials have hinted that the higher-than-targeted deficits may delay the national government's medium-term goal of achieving a balanced budget by 2003.

#### **PRIVATIZATION UPDATE: PHILPHOS SOLD ON SECOND TRY**

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The government offered for re-bid its 45% stake in heavily debt-saddled fertilizer firm Philippine Phosphate Fertilizer Corporation (Philphos) on November 22 after an earlier, unsuccessful auction the month before (October 25). In the earlier auction, the highest bid (P2.5 billion) fell 40% below the government's P4.2 billion indicative price. That price was unacceptable under privatization guidelines, which stipulate that the accepted bid should be no more than 20% below the government-approved ballpark figure. For the re-bidding, the government lowered its indicative price to P3.78 billion and eased payment terms (i.e., P2 billion by December 2000 and the balance payable over two years). Only one bidder showed up for the second auction -- the same group which offered the highest price on October 25. That group upped its earlier bid to P3 billion which, about 20% lower than the revised indicative price, the government considered as a "valid offer". (Comment: Regulations also allow the government to accept a sole bid after a previous unsuccessful auction. End Comment.) The Republic of Nauru, Philphos' other major shareholder, reportedly has waived its right to match the winning bid. The government had been trying to rid itself of Philphos since the Aquino administration launched a comprehensive privatization program in late 1986.

The sale of the government's stake in Philphos is likely to be the last privatization deal this year. The lives of the Committee on Privatization (the cabinet-level body tasked to oversee privatization efforts) and the Asset Privatization Trust (APT, one of the major disposition entities which took over the "non-performing assets" of financially restructured government financial institutions in the mid-1980's) officially end this

December after several extensions. As provided under privatization laws, unsold financial assets being managed by the APT will be transferred to a government financial institution and physical assets to the national government. COP officials expect the privatization program to continue under a "successor" office in the new year (performing basically the same functions as the COP and likely manned by the same technical group).

The expected P2 billion proceeds in from Philphos' sale will raise 2000 privatization revenues to barely P4.5 billion by yearend -- a far cry from both the original (P22 billion) and downward-revised (P13 billion) privatization revenue targets. The expected revenue from the recent sale faces some erosion by the recent, temporary suspension (November to January) of the 3% tariff on oil products (Manila 7266). The government expects to forego P1.1 billion in revenues over that three-month period (P367 million monthly or about P730 million during the last two months of 2000).

#### **PNB -- TAN WANTS OUT OF PURCHASE DEAL**

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It looks like Lucio Tan -- who has forfeited a P600 million down-payment for the government's 62 million shares in Philippine National Bank (PNB) -- has no intention whatsoever of putting up the P5.6 billion balance to consummate the deal. Tan had offered to purchase the government shares at a P100/share installment-price in July (10% down-payment and the balance payable over two years). At that time the government's 62 million shares were equivalent to a 30% stake in PNB. After making the down-payment, Tan reneged on opening a standby letter-of-credit (the government-required security for the balance). The government's ownership control in the commercial bank has since declined to 16% after PNB's P60/share stock-rights offering in September, during which Tan's group emerged as the major subscriber.

As a compromise to a potentially protracted and expensive legal battle, Department of Finance (DOF) officials had been trying to work out a "call" and "put" option with

Lucio Tan. The "put" option, in effect, would hold Mr. Tan to purchasing the government shares (net of the earlier down-payment) if the shares were not successfully privatized within a given period. DOF officials told the Embassy that Tan's group turned down the "put" option in a meeting with government officials last week, but agreed-in-principle to a five-year "call" option. The government is drafting the details of that agreement. That option would give the government a chance to regain 30% control of PNB -- hopefully to make the block more attractive to future buyers -- by allowing the government to purchase from Tan the 52 million or so shares which it had bypassed (and Tan had purchased) during September's capital-raising exercise. If exercised by the government within the first three years, Tan reportedly agreed to sell the shares to the government at P60/share at no carrying cost. If exercised within the last two years of the call option, Tan reportedly is agreeable to selling the shares at P60/share plus carrying cost (computed after the third year and based on the 91-day T-bill rate).

PNB shares are currently trading in the stock market at under P40/share and prospects on making money from the call option will depend heavily on the results of PNB's ongoing rehabilitation. If the government eventually chooses to exercise the call option, the government will have to find a way to raise at least P3 billion for the transaction. The government could, alternatively, consider selling its call-option rights, according to DOF officials. For now, however, the government's only consolation is that it is P600 million "richer" (from the deposit Tan forfeited).

#### **BANKING NOTES**

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**HSBC:** Early in the week, Hong Kong and Shanghai Banking Corp. (HSBC) -- one of the first banks to put up a foreign branch in the country -- formally signed an agreement with Equitable-PCI Bank to purchase one of the latter's savings bank subsidiaries (i.e., PCI Savings Bank) for P1.1 billion (about \$22 million). HSBC's acquisition of the thrift bank had initially posed legal questions under the "one-mode-of-entry" provision of the 1994 Foreign Bank Liberalization Act (i.e., to operate as

a foreign bank branch or to acquire or establish a majority-owned local subsidiary). In October, the Bangko Sentral ruled on the legality of HSBC's planned purchase of the thrift bank as an "investment" allowed by HSBC's "universal banking" license (which, under Philippine law, allows a bank to perform investment banking activities in addition to commercial banking functions). HSBC plans to continue operating the thrift bank -- to be renamed HSBC Savings Bank (Philippines) Inc. -- as a separate entity to strengthen HSBC's retail-banking operations in the country.

**Chinatrust:** Subject to approval by Philippine and Taiwan regulatory authorities, Chinatrust Taipei -- which owns 60% of publicly-listed commercial bank Chinatrust (Phils.) Commercial Banking Corp. -- announced that it had entered into an agreement with a group of local shareholders to purchase some 34% of the domestic commercial bank's shares. Chinatrust Taipei (Taiwan's largest private commercial bank) also intends to make a tender offer for the remaining shares, as required by Philippine regulations. Chinatrust's acquisition is being made under the provisions of the Philippines' new General Banking Law (GBL, signed in May 2000). The GBL opened a seven-year window during which foreign banks could own up to 100% of a domestic bank (with no requirement to divest) -- a relaxation of the previous 60% foreign-ownership ceiling provided under the 1994 Foreign Bank Liberalization Act. At least one other foreign bank, the Development Bank of Singapore (DBS), is working to buy-out its local partners (in DBS Bank Philippines).